KPMG

Covid-19: Impact on valuations

Recommendations and guidance from deal advisory experts

April 2020

Exhibit
7

DX-020

Executive summary

The recent Covid-19 outbreak and subsequent lockdowns have significantly impacted global markets with increased volatility and business disruption worldwide. When it comes to valuation, concerns have been raised about the fair value of companies, resulting in increased regulator and stakeholder scrutiny.

While it is difficult to predict the economic impact of the crisis with any degree of certainty, you may be seeking guidance and recommendations on valuing companies at this time. This report aims to help you ensure that your valuations, in so far as is possible, take the economic impact of this crisis into consideration.

Five essential recommendations for valuation

1. Increase the frequency of your valuations and reporting as appropriate in response to increased scrutiny by regulators and shareholders.

2. Assess the going concern status of your company based on what is known and knowable at the valuation date. The current uncertainty may be reflected in higher counterparty risks, covenant breaches and increased financial liquidity issues.

3. Consider company specific premiums and liquidity risks in your discount rates. Greater market volatility and high levels of uncertainty in the recent past may mean higher betas and debt margins. It is, however, too early to assess the long-term impacts.

4. Consider scenarios adjusted based on market evidence in your business plans and financial metrics by integrating what is known and knowable at the valuation date.

5. Widen the range of your valuations and monitor your assumptions regularly. The ranges themselves may be subject to volatility as the regular valuations you are performing will rely on projections that are subject to constant change. Robust documentation procedures are required as valuations may be performed based on assumptions that that may no longer be valid in the future.

Executive summary

IN THIS REPORT

ECONOMIC IMPACT OF COVID-19

1 | ECONOMIC IMPACT ON THE EUROPEAN MARKET

- The Euronext 100 dropped by somewhere between 20-25% between 1 January and 31 March 2020.
- The ECB plans to inject more liquidity into the system.

2 | ECONOMIC IMPACT BY INDUSTRY

- The industries the most affected by the Covid-19 crisis are travel and leisure, energy and resources.
- The industries the least affected by Covid-19 are consumer staples, information technology and common equipment.

3 | ECONOMIC OUTLOOK FOR THE NEAR FUTURE

- As it stands today, the true impact of the crisis is impossible to measure: current market conditions may only be temporary, and it is difficult to estimate the time required for economic recovery.
- According to a recent Oxford Economics study, in the first quarter of 2020, the global economy is expected to have contracted at a faster pace than during the global financial crisis in 2008.

IMPACT ON BUSINESS VALUATIONS

1 | VALUATION RISK FACTORS

- Volatility in global markets may lead to higher betas and debt margins. Uncertainty of business specific cash flows.
- Certain cash flows may not be as reliable or secure for businesses.
- Counterparty risk may potentially be higher as refinancing issues, covenant breaches, greater liquidity risks and greater risk of insolvency will result in higher risk of impairments.

2 | VALUATION CONSIDERATIONS

- Greater uncertainty can lead to a greater number of risks. This in turn creates a need for higher returns and lower asset values.
- Assessing the going concern status of companies is crucial.
- Consideration of the short-term, medium-term and long-term impacts of the crisis is also essential.
- To avoid issues, companies can monitor macro assumptions, valuation ranges, sensitivity analyses and scenario analyses on a continuous basis.
- Regular reporting and impairment analyses and robust documentation are required.

3 | VALUATION ADJUSTMENTS

Income approach

- Adjust business plans, cash flows and discount rates for additional risks not already considered in your valuation.
- Avoid the double counting of risk in both cash flows and discount rates.

Market approach

- Consider maintainable earnings in your market approach by, for example, excluding one-off items.
- Ensure the multiple is congruent with the metric to which it is applied.
- Assess whether the market approach is no longer appropriate for recent transaction prices, especially that date back to before the pandemic began.
- Avoid the double counting of impacts on metrics and multiples.

OTHER

- Reassess liquidity risks, covenant breaches, etc.
- Reassess the credit quality and repayment risk of debt investments.

4 | HOW KPMG CAN HELP YOU

- Tackle Covid-19 valuations together with KPMG, and our highly experienced team of 50 deal advisory professionals.

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The economic impact of Covid-19

The economic impact of Covid-19

These unprecedented times do not only bring serious threats to the world's health, but also a number of economic challenges.

In this section, we address the following questions:

1. HOW HAS COVID-19 AFFECTED THE EUROPEAN MARKET?

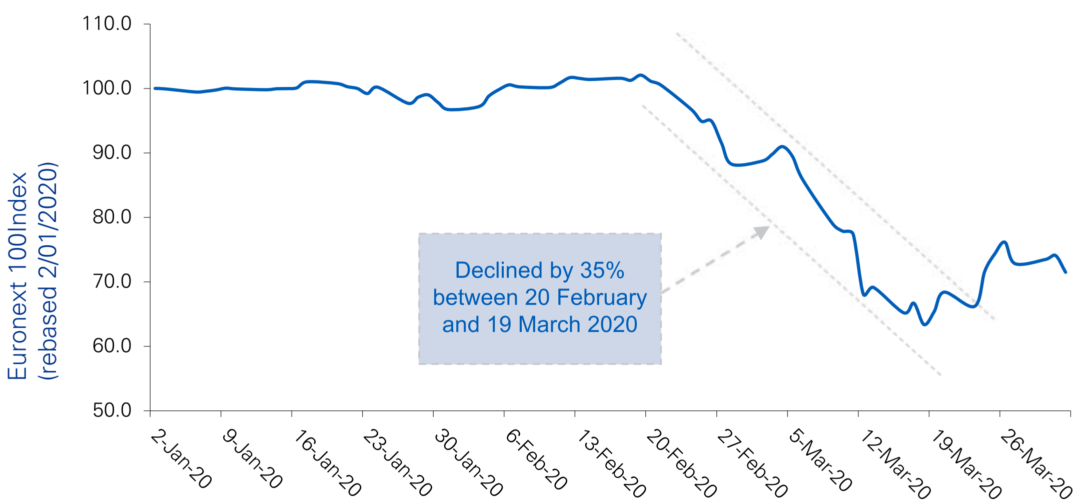
2. WHICH INDUSTRIES ARE THE MOST AND LEAST AFFECTED BY THE OUTBREAK?

3. HOW DOES THE NEAR FUTURE LOOK?

1. HOW HAS COVID-19 AFFECTED THE EUROPEAN MARKET?

Between 1 January 2020 and 31 March 2020, the Euronext 100 index fell by somewhere between 20 and 25%. The first triggers for this sharp decrease came between 20 and 23 February 2020—the Italian Government placed towns in the north of Italy in lockdown, and Iran and South Korea recorded significant increases in case numbers. When the WHO then elevated the virus' status to a pandemic, market conditions worsened across the globe. Stock markets started to decline, and from 20 February to 19 March, the Euronext 100 index dropped by 35% before recovering slightly on 26 March.

The impact of Covid-19 on the European market



To counter the economic impact of Covid-19, and mitigate the effects on the European economy, the European Central Bank (ECB) announced that it will be injecting liquidity into the banking system on more favorable terms than usual. The Fed and Bank of England also announced measures to pump additional cash into their respective markets.

Source: Capital IQ, KPMG analysis

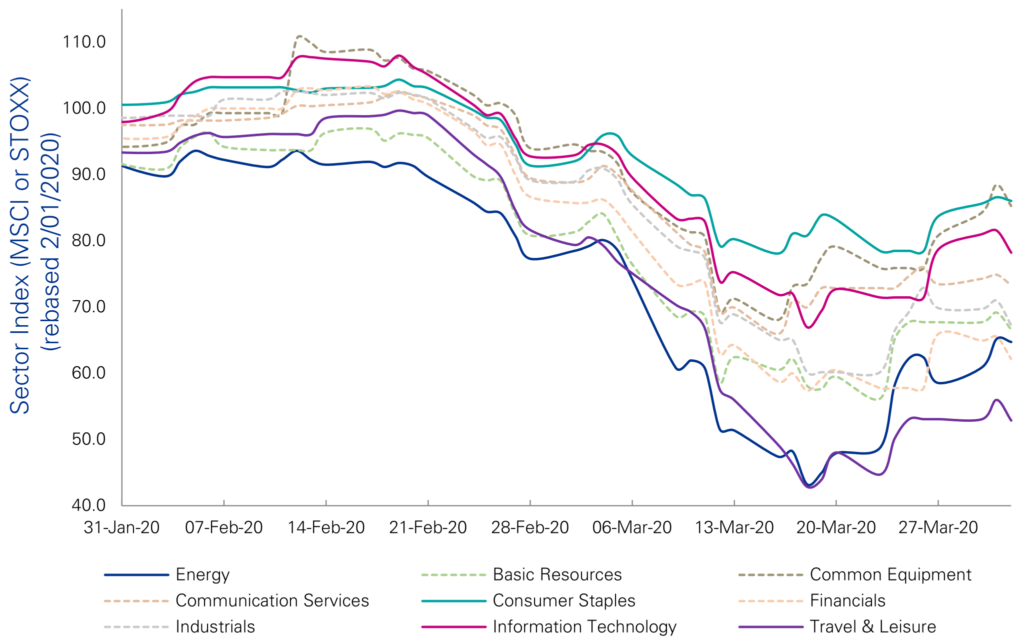
The economic impact of Covid-19

2. WHICH INDUSTRIES ARE THE MOST AND LEAST AFFECTED BY THE OUTBREAK?

Below you can see how a number of key European sector indices evolved between 1 February and 31 March 2020. The market indices show a general decline with certain sectors affected more than others.

The industries most affected by the Covid-19 crisis are travel and leisure, energy and resources—mainly as a result of the lockdown measures and travel restrictions introduced worldwide. Conversely, consumer essential industries such as consumer staples, information technology and common equipment are least affected by the crisis..

The impact of Covid-19 by industry



Source: Capital IQ, KPMG analysis

3. WHAT IS THE ECONOMIC OUTLOOK FOR THE NEAR FUTURE?

The World Health Organization declared a global health emergency at the end of January 2020 and global markets started to feel the heat in February 2020.

As it stands today, the true impact of the crisis is impossible to measure: current market conditions may only be temporary, and it is difficult to estimate the time required for economic recovery. Recent market movements and the macro-economic measures adopted by different institutions (including the Fed) show similarities with the global financial crisis (GFC) of 2008.

According to a recent Oxford Economics study, in the first quarter of 2020, the global economy is expected to contract at a faster pace than during the GFC in 2008. Global growth in 2020 as a whole is expected to be around the zero mark. Further to this, the Eurozone's GDP for 2020 is expected to contract by around 2.2%.

Source: World Economic Prospects March 2020 by Oxford Economics, KPMG

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Impact on business valuations

Impact on business valuations

Although, at this stage, the true economic impact of the crisis is still unknown, we have presented our initial thoughts regarding its impact on the fair valuation of businesses.

In this section, we address the following questions:

1. WHAT ARE THE PRIMARY FACTORS THAT IMPACT GLOBAL BUSINESS VALUATIONS?
2. WHAT SHOULD BE CONSIDERED WHEN VALUING A COMPANY?
3. HOW SHOULD VALUATION ADJUSTMENTS BE APPLIED?
4. HOW SHOULD ONE QUANTIFY ANY APPLICABLE ADJUSTMENTS?

1. WHAT ARE THE PRIMARY FACTORS THAT IMPACT GLOBAL BUSINESS VALUATIONS?

We have identified the most relevant factors and risks to be referred to when valuing a company:

VOLATILITY IN GLOBAL MARKETS	• We have observed significant market convulsions and increased volatility over the past couple of months, and this will impact valuations in the form of higher discount rates. These rates will likely rise along with debt margins and betas as investors become more risk averse.
UNCERTAINTY OF BUSINESS SPECIFIC CASH FLOWS	• On a company level, the uncertainty surrounding the true economic impact of Covid-19 has resulted in corresponding difficulties with business plan forecasting. Forecast estimates would usually take the impact of the crisis into account. However, without reliable economic forecasts available, companies will need to look to other company-specific risks so as to produce a reasonable business forecast.
FINANCIAL RISK FACTORS	• The ongoing operational and economic uncertainties will likely lead to an increase in counterparty risk, and we may see a number of companies defaulting on their outstanding obligations. This will further increase the risk of investing through counterparties that either operate in high risk industries or have low credit ratings. • Many companies are reporting a rise in liquidity risk as they find themselves unable to deliver on short-term obligations. Banking institutions have announced various measures aimed at maintaining a certain level of liquidity in the market. These measures are outlined in this report. • Due to these heightened risk factors, we will likely see a rise in debt covenant breaches, insolvencies and asset impairments in the short- snd medium-term.

Source: KPMG

Impact on business valuations

2. WHAT SHOULD BE CONSIDERED WHEN VALUING A COMPANY?

GENERAL VALUATION CONSIDERATIONS	• Greater uncertainty results in higher risk, which in turn justifies the demand for greater returns. This will ultimately result in lower asset values. • The short-, medium- and long-term impacts of the crisis, whether they be macro-economic or business-specific, will need to be taken into consideration. The market disruption observed today may be temporary, and the adjustments we make could potentially overstate or understate the crisis' impact on the company's valuation. • Fair value is based on what is known and knowable at the measurement date. The assumptions taken into consideration today may no longer be applicable tomorrow, which means that the procedures and rationale for any valuations you perform should be documented in full. • Assessing the going concern status of companies will also be key, so valuations should focus on companies' short-term cash flows and liquidity needs. • Existing valuation guidelines can help during times of uncertainty, notably: - 'Dealing with valuation uncertainty at times of market unrest' issued by the International Valuations Standards Council (IVSC) - 'Special valuation guidance' for valuations as at 31 March 2020 issued by the International Private Equity and Venture Capital Valuation (IPEVC)
AVOIDING SIGNIFICANT OVER/ UNDER VALUATIONS	• The following measures can help avoid significant over or under valuations: - The use of valuation ranges, sensitivity analyses and scenario analyses, such as modelling scenarios based on 6-, 12- and 18-month recovery periods. When two or more scenarios present themselves, you can present the most likely scenario in the valuation. - The continuous monitoring of macro-economic assumptions to ensure relevance to current market conditions. - The inclusion of any existing regular reporting and impairment analyses produced by the company.

Impact on business valuations

3. HOW SHOULD VALUATION ADJUSTMENTS BE APPLIED?

INCOME APPROACH

As we have already stated, fair value is based on what is known and knowable at the measurement date. As such, we recommend that companies estimate potential performance shortfalls for Q1, Q2 and beyond in so far as is possible.

- It may be judicious to consider adjusting your business to cater for performance shortfalls that result from supply chain disruption, volatility in commodity prices, workforce restrictions, temporary curtailment of operations, mothballed assets or delays in payments by your customers.
- Financial projections and metrics should consider any government incentives and short-term measures applicable. You can consult a list of the business support available in Luxembourg here.
- As investors become more risk averse, adjustments to discount rates in the form of additional risk premiums may become necessary. The income from these risk premiums may set off the financial impact of any other company risk factors which aren't covered in forecast cash flows or market indicators. Care should be taken to avoid any double counting of risks, for example additional risk premiums aren't required for factors that have already been addressed in cash flows or included in market inputs.

MARKET APPROACH

- When applying a market approach, ongoing metrics and earnings should be looked at on a market participant basis and therefore one-off impacts can be excluded. However, expected adverse performance in Q1 and Q2 2020 and beyond, if deemed one-time, would still impact cash balances and would be reflected as a deduction from enterprise value in estimating fair value.
- An appropriate multiple should be congruent with the metric to which it is applied. The percentage change in Market Capitalization of comparable companies may provide a good proxy for the magnitude of the change to be expected in the multiple.
- It may no longer be appropriate to consider application of recent transaction prices, especially those from before the expansion of the pandemic.
- Care should be taken to avoid any double counting with respect to downward adjustments (i.e. penalizing the metric as well as multiples considered).

OTHER ADJUSTMENTS

- Investors and companies may need to reassess liquidity needs (i.e., likelihood of a debt covenant breaches, impact of the extended reduced cash flow, funding of working capital required).
- A re-assessment of credit quality and repayment risk needs to be considered for debt investments.
- Emphasis needs to be placed on scenario analysis.

Source: KPMG, IPEV paper, IVSC paper

Impact on business valuations

4. HOW SHOULD ONE QUANTIFY ANY APPLICABLE ADJUSTMENTS?

TACKLING COVID-19 TOGETHER WITH KPMG

Valuations are notoriously complex during times of crisis, and require deep knowledge of a range of markets, geographies and industries. By working with KPMG, you can:

- Benefit from the combined knowledge and experience of over 50 deal advisory professionals based in Luxembourg.
- Access our pool of experts around the world to find the specific expertise and market knowledge you require to deliver the most accurate valuations possible at this time.
- Draw on our experience advising large corporations, private equity houses and other financial institutions during crises or challenging periods

The benefits of working with the KPMG team:

INDEPENDENCE AND CONFIDENTIALITY

EFFICIENCY AND ON-TIME DELIVERY

COST EFFECTIVE APPROACH

COLLABORATION AND OPEN DISCUSSIONS

TECHNICAL EXCELLENCE AND QUALITY SERVICE

FURTHER RESOURCES

To help you understand and respond to the rapidly evolving business challenges, we are sharing our guidance and insights. Stay informed and bookmark our resource page:

http://kpmginfo.lu/covid19

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